RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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July 7, 1993 **LETTER 1125**

PUMPING: The Fed buys bonds from the banks, credits the banks for the bonds, and these credits become "new dollars" that are literally manufactured "out of thin air." The so-called "Monetary Base" is made up of the debt that the Fed buys plus the currency. Over the last two months the monetary base has risen at a 16.7% rate. The Fed has its foot down hard on the monetary pedal, and in due time this will translate into inflation. But ironically, the Fed (which is actively creating the potential inflation) lets it be known that it is worried about inflation. Of course they're worried about inflation -- they've already sown the seeds for inflation. Ironic, isn't it?

QUESTION: Remember the movie, "Who's Killing the Great Chefs of Europe?" Well, we have its sequel. It's called, "Who's Killing the Great Stocks of America?" Answer: Darned if I know, but one by one they're getting knocked off. Wal-Mart, Procter & Gamble, Johnson & Johnson, US Surgical, Amgen, IBM, Apple, Merck, Eli Lilly, Bristol Myers, Halliburton, Gillette, Digital Equipment, Waste Management -- the list goes on and on.

And, of course, you know where the public is. They're loaded, super-loaded in mutual funds. So what's happening there? *Investor's Business Daily* runs their index of 20 leading mutual funds. This is interesting -- the Index is now only slightly above its peak recorded back in January, so my perception is that the typical mutual fund has gone nowhere in '93, despite the incoming billions of dollars from a semi-frenzied public.

One of the things that bothers me about this market (as most of you know) is the almost ridiculous proliferation of mutual funds. If Spain is in favor, three Spanish funds emerge, if dog food is hot, a dog food fund will come out of the woodwork. I mean, talk about dreaming up items for the public to buy, have you ever seen anything like this? It's getting so the newspapers need two pages just to list all the funds (and those are just the open-ended funds).

When the primary trend of the market finally turns decisively down, I would expect an absolute slaughter of the funds. It will be like 10 elephants trying to get through a three foot door all at the same time.

Meanwhile, I want to reiterate again what I see as the BIG PICTURE. I believe that financial assets (stocks and bonds) are terribly overvalued. Large investors, sophisticated investors, seasoned investors -- know values. Charles Dow said it almost a century ago. "To know values is to know the meaning of the market."

So to get back to the BIG PICTURE, in my opinion it's that informed investors are now quietly moving out of financial items and into real or tangible items. And the king of the real items is real money -- GOLD.

The Fed is obviously aware that the major prop under the stock market is low, low interest rates. The reason the Fed is so worried about inflation is that if inflation does flare up, the Fed will (at some point) have to fight it by increasing interest rates. If that happens, the overvalued stock market will topple over.

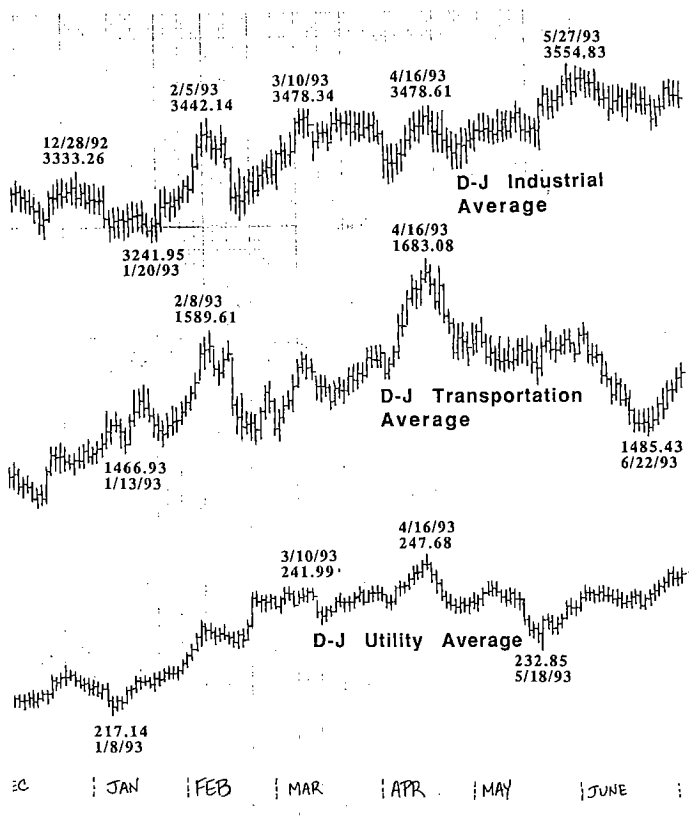
So the Fed is walking a fine line, creating potential inflation and at the same time hoping against hope that it doesn't materialize. Gold is the merciless barometer that the Fed fears. My guess is that if gold goes over 400 the Fed will be frightened and will be forced to raise rates. So this is the great unseen, unspoken game that is being played. And you can see why the "government" takes every opportunity it can get to talk down gold.

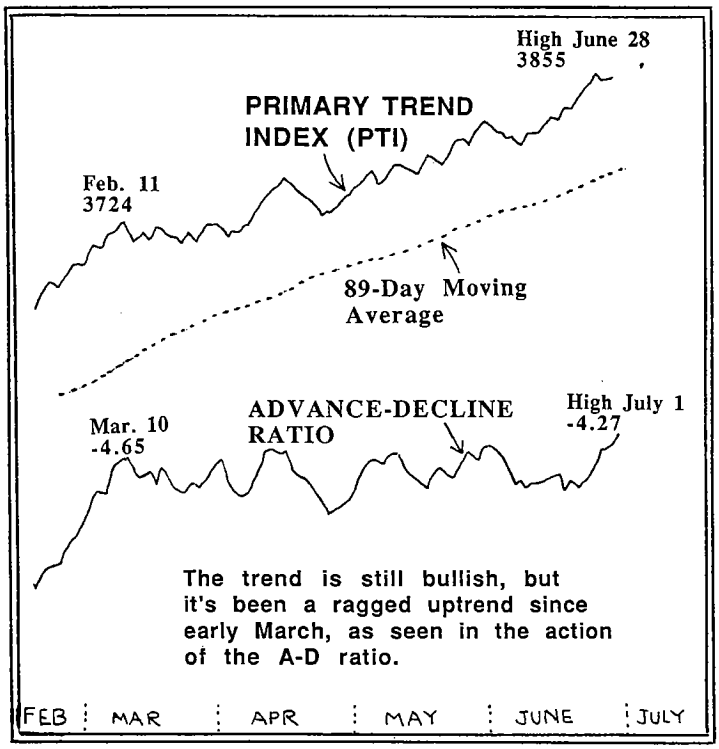
June 25 DJIA 3490.89; PTI 3847; A-D Ratio -4.83
July 1 DJIA 3510.54; PTI 3853; A-D Ratio -4.27
Dow Yield: 3.15%; Dow Price/Earnings: 31.8
Dow 200-day MA: 3357; Dow 30-day MA: 3506
Dow Times Book Value: 2.68; PTI 89-day MA: 3794
Percentage of Undervalued Blue-chips: 6%
Low Risk Buy Index: +60

The ignorant media joins in on the gold-bashing. On June 29 the *WSJ* headlined its column, "Gold Tumbles Two Dollars." Mind you, not gold backs off two dollars or gold retreats two dollars, but it "tumbles" two dollars. No matter, the next day gold staggered up 3.50.

Meanwhile, the primary trend of the stock market continues bullish. I pointed out in the last Letter that although the Transportation Average had broken down, the Dow was continuing to hold ABOVE its preceding decline level. That level is **3443.01**. Thus, a downside non-confirmation existed, and the stage was set for a rally (although I said that I thought it would be a weak rally).

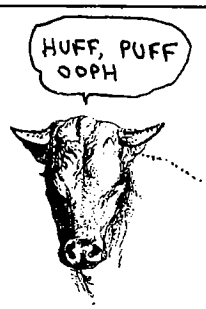
The rally materialized. The Dow (see page 1 chart) has pushed into the 3500 plus area, and my Primary Trend Index (PTI) again advanced into new all-time high ground. As I've said many dozens of times, the real trouble won't be upon us until the PTI turns down, drops below its 89-day moving average, and traces out a decisive declining trend. That just has not happened yet.





The advance-decline ratio continues in its "Buying Stampede" mode. Incredibly, since October 9 the ratio (see page 2 chart) has refused to back off as much as one full point. Thus, the Stampede has been in force for over eight months. The A-D ratio hit a peak in early March, and it has been moving generally sideways ever since. Nevertheless, it's amazing that it has refused to give up one full point.

INVESTMENT POSITION: Just in case you missed it, the Percentage of Undervalued Blue Chips (as monitored by *IQ Trends* here in La Jolla) has dropped to its lowest level on record --down to 6%. This means that of the 350 blue chip stocks which *IQ Trends* follows, only 21 stocks out of that entire 350-stock universe are undervalued. Which is another way of saying that the stock market is overpriced, way overpriced, dangerously overpriced.



Let me put it this way -- if you think you're "investing" when you buy a stock or a mutual fund today, you're in dreamland. What you're doing is gambling that some fool out there will pay more for your stock or fund than you did. Good luck.

I don't want to bore subscribers but what I do like here are the gold stocks. The following are my choices. American Barrick and Placer Dome and Echo Bay (Amex) appear to be leaders. Pegasus (Amex) acts well. I like Royal Oak (Amex), and I like Agnico Eagle (NASDAQ). I also like Newmont Mining and Newmont Gold. I bought some LAC Minerals last week. I like Hemlo Gold Mines (Amex). Horsham (its price is around 12) owns 13 bucks worth of Amer. Barrick plus Clark Oil plus some expensive acreage in Berlin.

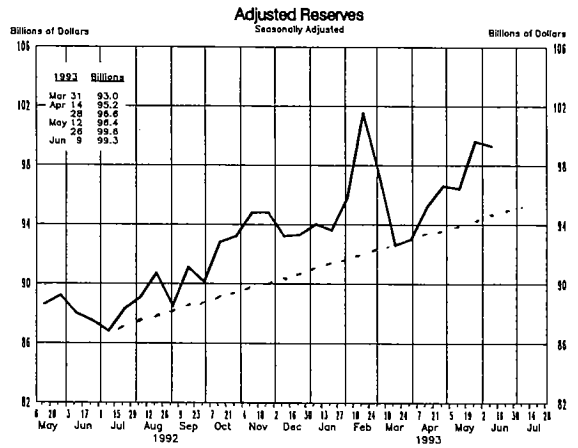
You don't have to be slick or cute or even terribly smart to get in on the gold market. You just have to MOVE. And I'll admit that isn't always easy. It isn't easy because most people like to "read the good news" before they invest. The problem is that by the time the good news is out, the stocks have made a large portion of their move.

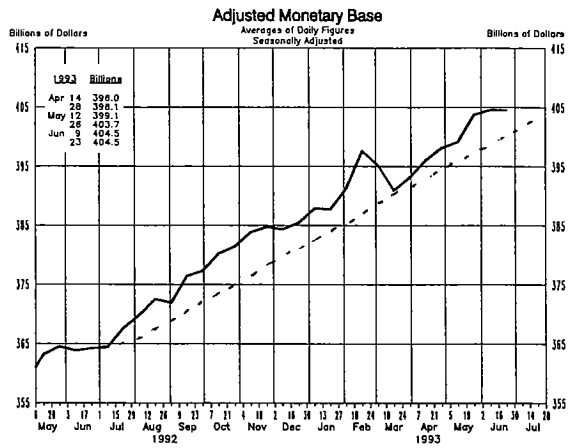
Well, that isn't strictly true. In a real bull market, the good news gets better and better, and finally the news becomes irresistibly good, and that's about the time the public enters the market. They call that the third phase of a bull market. And many stocks do record huge moves during the third phase. But even so, it's comforting to have entered the bull market near the bottom than during the frenzied third phase.

LOOKING AHEAD: THE UNEMPLOYMENT CURSE: In the last Letter I outlined the reasons why I thought the number one problem for the '90s was going to be unemployment, and I mean global unemployment. I also wrote that the governments of the world would move to fight the politically poisonous effects of unemployment. The basic tool of the battle against unemployment would be fiscal stimulation on a massive scale, meaning expanding money supplies, declining interest rates, currency devaluations and inflation.

THE TAX CURSE: Now let's go into a bit more detail. Let's assume that most of Clinton's so-called "deficit reduction" package will pass the House and Senate. At that point the nation will be faced with a barrage of new taxes. Then as *Sindlinger* writes in his latest report, *"Economic history records that, since the time the snake enticed Eve to eat the apple, no nation has ever created an economic recovery on rising taxes . . . Political history records that, since Adam lost a rib, no politician was ever elected or re-elected as an incumbent on a promise to raise taxes. Remember Walter Mondale and then there was George Bush with his 'read my lips.'"*

THE SQUEEZE: So the US will be cursed with across-the-board higher taxes. Consequently, I have to think that the US economy is going to have a hard time over the next few years. The Clinton tax boosts will have the effect of draining capital from the private sector and transferring it to the inefficient and wasteful government sector. The businessman, the entrepreneur, the saver, the

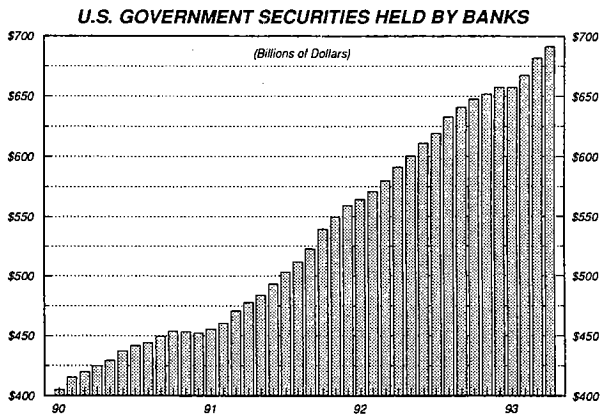




executive, all will be squeezed, disheartened and bitter. The US economy will be operating with the brakes on.

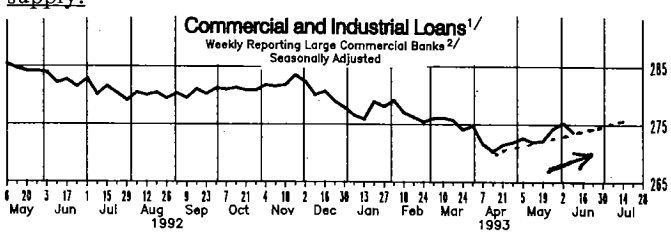
FED TO THE RESCUE: This is where the Fed comes in. Fed stimulation (or I should say MORE stimulation) will be the nation's hope. But let's not kid ourselves, the Fed has already been working overtime. For the past three years the Fed has been pumping up bank reserves. You're skeptical? Study the two charts on page 2, courtesy of the St. Louis Federal Reserve.

Up to now, although the banks have been brimming over with reserves, the broader money supply has been going nowhere. The reason -- instead of loaning out the money (thereby expanding the money supply), the banks have been buying Treasury paper yielding almost 7% while at the same time they have been paying out only 3% for savings accounts or CDs. It's been a highly profitable game, and it has accomplished one goal -- it has reliquefied the banks.



The money supply is a product of bank lending. If the banks don't lend, the money supply doesn't expand. This is the problem that's driven Alan Greenspan up the wall. No loans, no monetary expansion. And all the while the Fed's been frantic to boost the money supply.

THE COMING INFLATION: The accompanying chart is one I've run before. It shows the path of the banks' Commercial and Industrial Loans. Note that since April, for the first time in years, the trend of Bank Loans is finally heading higher. This new development is going to mean a rising trend in the nation's money supply.



EXPANDING MONEY SUPPLY FIGHTS THE TAX SQUEEZE: As Clinton's tax squeeze hits, there will be a dampening effect on the economy. The Fed is well aware of the deflationary pressures that will be generated by higher taxes. The Fed will move to pump up the money supply, pump it up more frantically than ever in an effort to offset the stifling effect of the tax boosts. The net result --monetary inflation.

THE COMING FLIGHT OUT OF BONDS: The massive liquidity now flooding the banks will slush over into the economy, and the nation will be faced with both monetary and price inflation. The purchasing power of the dollar will decline drastically. Consequently, investors will want to get out of bonds. The public, already up to their eyeballs in bond funds, will panic. Declining bond prices will translate into higher long-term rates, and thus the Fed will have another fight on its hands.

MONETIZATION: To fight higher rates the Fed will be forced to buy bonds at an accelerating rate. This process is called monetization of the debt, and it is inflationary. Actually, the Fed has been buying bonds at a fairly rapid clip over the last few years. Statistic: In the past two-and-a-half years the Fed has bought $62 billion in bills, notes and bonds. Incredibly, this $62 billion is actually greater than the nation's GDP, which had risen only $57 billion over the same period. Seasonally adjusted, the Fed has been buying bonds at a 12% rate.

As William Fleckenstein writes in his great June 14 *Barron's* article, *"In a Democracy all roads lead to inflation. Can we help choosing leaders who overpromise and overspend? It goes against human nature and political expediency to defend paper money or assets at the expense of voters suffering in a recession . . . Now that the world is choosing again to be led by the United States, falling interest rates and competitive devaluations have become the standard economic fare worldwide . . . The death of price inflation has been greatly exaggerated. In fact, we have already bought a new round of inflation. Only the precise timing and ultimate degree remains to be discovered."*

Under these circumstances, there will remain only one asset of choice. That asset will be gold. As I've said before, this is the very early part of the resumption of the gold bull market. This is an accumulation phase, the phase where informed investors take their position in the metal and in the stocks.

GOLD DISCOUNTS: Today, ironically, gold disclaimers warn, "There is no inflation, so why in the world would anyone want to own gold?" The answer, of course, is that the gold market, like the stock market, does not trade on what we saw yesterday or what we see today. The gold market discounts, it looks ahead. If inflation was rampant today, every fool and his brother would be buying gold. Inflation is not apparent today, only the seeds of inflation are apparent.

The time to buy gold is when the reason for buying it is not obvious. If you wait for monetary inflation to arrive before buying Homestake or Placer Dome, you will be like the fellow who sneered at Microsoft in 1980, because computers were newfangled gadgets, and nobody could figure out how to really make any practical use of them.

NOTES & QUOTES: The Big Mystery: Why? Why? Why are the Democrats doing it? Clinton's tax increases won't bring as much money as he hopes it will, and Clinton's "future spending cuts" are more fantasy than fact. The federal deficits are almost guaranteed to increase, and the voters will rebel against the new sky-high taxes. So what's going on? Do the Dems have a death wish or what?

My answer is that the Dems are stuck with Clinton and his nutty package. If they vote it down, they'll have destroyed the Administration. The Dems' only hope -- still lower interest rates, maybe 6% on the long bonds and 2% T-bills to wake up the economy. Will Greenspan and the Fed cooperate? There's a good chance they will, given the fact that factory orders have declined for four months running, the leading indicators are down again, and consumer confidence is swooning.

But why have the Republicans come up with such lukewarm, muffled opposition? My guess -- they secretly want the disastrous Clinton "tax-pact" to pass. It's the Republican ticket to a sweep in '96 and '98.

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And you thought you were rich. Let's say you're now making $1 million a year. The current tax (single, no deduction) is $305,300. On $3 million the current tax is $925,300. Then of course there are state and local taxes.

But under Clinton's proposed tax-pact the tax on $1 million would be $376,500. And the tax on $3 million rockets up to $1,168,500. If you live in California or New York or a high-tax state, then under Clinton you will pay total taxes of almost half of what you earn. On top of that, if you're an actor or an athlete you have your

agent to pay and maybe a manager. But why be depressed -- think of how much the government gives you in return for all your taxes.

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Jack Kemp (former Bush cabinet member and former San Diego Charger quarterback) says that Clinton's taxes will cost the US 4 million jobs over the next three years and "will absolutely destroy the Northeast." Kemp, who will probably run for president in '96, says that the Clinton taxes zero in on people who work, save and invest in new jobs. He states, "You can't have capitalism without capital." He adds that Clinton will raise the tax rate on capital formation by 40%. "His tax plan," says Kemp, "will destroy his presidency, it will elect a Republican Congress in '94, in my view."

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How about Hillary's "stealth-health" plan? Russell opinion: It's too damn expensive, the majority of Americans don't want it, it's dead for '93 and with an election coming up in '94, it's dead for '94 as well.

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I've often said very nice things about that wonderful newspaper, the *International Herald Tribune*. And do you know what those nice people did, they gave me a free subscription. But in all honesty, I like this paper so much that I'd be happy to pay the $377 it costs to receive it daily outside of NYC. In NYC it's $357. The paper is truly international, and you can contact them at (800) 882-2884. If I had my choice of only four newspapers I'd pick the *New York Times*, the *International Herald Tribune*, the *Wall Street Journal*, and *Investor's Business Daily*. Next choices would be the *Christian Science Monitor, USA Today*. The *Weekly Washington Post* is also a winner (contains the best articles from the daily *WP*).

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Lloyd's of London, probably the world's most famous insurance company, announced the largest loss in its three centuries of history -- $4.33 billion. Its 30,000 investors are angry and shocked, and many of them stand to go broke (they are partners and are responsible for losses). The investors stand to lose an average of $148,000 each. Thousands of so-called "Names" in the US are suing Lloyd's claiming fraud and negligence and also claiming that Lloyd's put them into risky investments while keeping the safe ones for Lloyd's insiders.

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A seat on the NYSE sold recently for $650,000. The bid-asked spread is a bit wide -- the bid is $575,000 and the asked is $950,000.

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A lot of people asked me whether I rode my Harley to the monster Harley 90th anniversary party get-together in Milwaukee a few weeks ago. The answer is "No, I didn't, darn it, but I would love to have gone." Harley Davidson motorcycles are one of the great American treasures. They've beaten the Japanese silly in the big bike classification. Every time I take one of my three Harleys out, people come up to me and ask if it's for sale. Harleys have been around since 1903, and today they are wanted around the globe.

Here's a bit from the *Chicago Tribune's* description of Harley's 90th anniversary parade into Milwaukee: "Tens of thousands of Harley Davidson motorcycles roared into Milwaukee from several directions as thousands of Milwaukeans cheered, gave high fives and waved at them from overpasses along sides of Interstate 94. American flags were as pervasive as on the Fourth of July. From one overpass south of the city, a firetruck had extended its ladder straight up, and a huge flag flapped in the breeze as a double column of tens of thousands of Harleys rumbled beneath them from the staging area in Kenosha . . . And then something happened, something people have a hard time putting into words. Somehow, as the hands and flags waved and high fives were extended . . . an unforeseen meaning emerged from the columned spectacle of the throaty, rumbling motorcycles, wheeled symbols of individuality, and freedom holding tight, rolling in rough formation: 'I've never seen more grown men crying than I did on Saturday,' said Ken Schmidt, a Harley employee. Said Bill Trapp, a Milwaukee County Sheriff, 'Those of us who were there will never forget it as long as we live.'" By the way, note that Harley stock (much recommended here) has just rallied to an all-time high above 41.

Then there's the huge annual (August) Harley bash in Sturgis, S. Dakota. But if I went to Sturgis, I might be tempted to move there. Listen to this: S. Dakota has (1) no corporate income tax, (2) no personal income tax, (3) no personal property tax, (4) no pollution, (5) no traffic tie-ups, (6) almost no crime. Only one problem -- it gets mighty cold in S. Dakota, and those winters are awfully long.

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The poor old genius, Thomas Jefferson, left the presidency bankrupt. That was an embarrassment and a shame for a former US president. But don't worry, it doesn't happen today. Take George Bush and Ronald Reagan. They're both millionaires and each receives an annual pension of $148,000. On top of that, the Republican National Committee has paid Reagan $12,500 a month towards maintenance of his LA office and Bush's Houston office gave him $50,000 to cover his first four months in private life. There's more -- this year the government (your's and mine) will give Bush $463,000 and Reagan $633,000 to cover office, rent, staff and travel. Yep, no more bankrupt presidents, as you can see.

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France, chaffing under German leadership, is toying with the idea of pulling out of the ERM (the European currency union). France notes that Britain pulled out, dropped its interest rates, and is now showing signs of recovery. Will France follow Britain? If they do, it will END hopes for a European monetary union.

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The global recession is exacting its toll on the world's leaders. In France, Mitterand's approval rating has dropped to 41%, in Canada Kim Campbell's is down to 37%, in Germany Kohl's has slumped to 26%, in Britain Major's has collapsed to 16%, in Japan Miyazawa is hated with a minuscule 9%, and here in the US Clinton is at an embarrassing 37%.

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One very very visible sign of the vicious European recession -- car sales in western Europe have dropped 17.9%; for the first five months of 1993 there's been a sales decline of over a million cars.

Meanwhile, Jose Ignacio Lopes de Arriortua (he was GM's cost cutting genius until he left a few months ago) is now working for Volkswagen. His plan is to produce the world's lowest cost (to manufacture) and cheapest car. No location has been picked yet for the new "killer plant," but rumors have it that it will be in the Basque area of Spain. So it's now up to Volkswagen -- will they actually go ahead with the plant? We should know soon.

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Real estate has been hit hard in California, but they're still not giving houses away here. For instance, singer Bobby Vinton has just put his 113-acre Malibu ranch on the market. Asking price $20 million. And Whoopi Goldberg just bought a house that was recently on the market for $3.4 million. Whoopi got a bargain -- she paid $2.5 million for it. Whoopi started out years ago in San Diego, doing her comedy act for peanuts in local coffee houses. And that brings back memories -- I owned a coffee house in San Diego during the late '60s and early '70s. Steve Martin used to come down with Jackson Browne and they'd play for nothing, just for the exposure. Martin had a great comedy act in those days. He still does but now he gets paid.

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Doctors and scientists are beginning (finally) to take vitamin supplements seriously. Latest thesis is that large doses of vitamin E (800 mg. or more daily) will reduce the incidence of heart attacks. I've been doing that for years, and I'm still around. A lot of subscribers seem to be worried about my health. They call here and ask, "Is Mr. Russell all right?" Answer: I'm all right. Last week a subscriber wrote to tell me that aluminum will shorten your life. He said avoid aluminum cooking pots. I've heard this before, and I take it seriously. We cook in stainless steel, which I think is a better metal anyway. He says avoid drinks (beer, pop, fruit juices) in aluminum cans -- buy them out of glass containers. By the way, I remember the nickel cokes and soft drinks of my boyhood. In my opinion, the biggest rip-off and waste of money (outside of gambling) that I know of is the soft drink. A can full of chemicals for 50 to 75 cents that cost probably less than two cents to produce. Learn to drink water, it's better for you and a lot cheaper (unless you indulge in that other rip-off, bottled specialty water from "pure mineral springs").

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The Clinton "family" history is truly sad (is this the ultimate nuclear family?). Clinton's natural father died in an auto crash just weeks before Clinton was born. His step-father died following three marriages, the last to Clinton's mother, Virginia Kelley. Kelley married three other men, one of them twice. The family says that Clinton has six step-siblings and at least one half brother, the struggling "singer," Roger Clinton. Now it turns out that a Henry Ritzenthaler, 55, is probably Clinton's long-lost half brother. Whew.

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The right to die, the right to live in a safe neighborhood, the right to good medicine, the right to strike, the right to a job, animal rights, kids' rights against parents, grandparent's rights against parents, on and on. If you want anything these days, just tack a "right" on it. As columnist John Leo writes, "Here's a modest proposal. Let's try to go a whole year without inventing any new 'rights.'"

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Is this possible? Columnist Malcolm Berko notes that "The Dade County Commission (Miami) just enacted legislation that requires the Spanish language to be used in conducting all government business, in effect replacing English as the mother tongue in South Florida." Berko says, stay out of Miami and he suggests that you spell Miami backwards ("I maim" for people who can't spell).

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Gosh, what's football coming to? Football's Philadelphia Eagles couldn't sign their number one draft pick, giant 305-pound lineman Lester Holmes. Lester missed rookie camp, and that made the Eagles really mad. So the Eagles wrote a letter to Lester's mother telling her that Lester was "making a big mistake." But Lester intercepted the letter. "I was humiliated," complained Lester. I'll bet he was, but I'll bet he's also avoiding mama.

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Some of the toughest movie reviews are put out by *Daily Variety*, the industry newspaper. *DV* is read by exhibitors and everyone in Hollywood, so they have to "tell it like it is." And they don't kid around. Here's their review of "The Last Action Hero," Columbia Picture's Schwarzenegger epic. "Last Action Hero is a joyless, soulless machine of a movie. This $80 million-plus mish-mash of a fantasy, industry in-jokes, self-referential parody, film buff gags and too-big action set-pieces will test the clout of a humongous, super-star driven marketing campaign to put over a picture people won't like, with the possible exception of early-teen boys. After the big opening, word-of-mouth will likely send box-office down a steeper-than desired slide."

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Zoos are changing. They are no longer a collection of fat, bored animals sitting in cages too small for them. The new zoos feature natural surroundings, large tropical settings, and educational exhibits. American zoos now have more visitors (over 100 million a year) than the annual attendance of all the basketball, baseball and football games taken together.

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Talking about attendance, the 1893 Columbia Exhibition in Chicago (really a world's fair) holds the all-time attendance record for a single event -- 27 million visitors.

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Ah, the Russians. *The Financial Times* reports that the Russians are now pledging metals from their stockpiles, "everything including rare earths and aluminum" as collateral in their urgent quest for hard currencies including dollars.

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Only in San Diego: Sheriff's deputies and firemen gathered at a bomb-disposal site to set off thousands of illegal fireworks. It was done in front of the media and the firemen lectured about the dangers of careless fireworks. Unfortunately, a spark set off a 10-acre brush fire, which had to be fought with 50 firefighters, a bulldozer and two water-dropping helicopters.

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Hard times at Hollywood. No longer are the chic expensive restaurants the place to go for Hollywood's big brass at lunchtime. The new eating places are the studio commissaries, where the producers and stars "do lunch" at bargain prices.

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The Arts & Entertainment channel aired a marvelous program on the "Greatest American Cars of the 20th Century." Here's the list in the order they were presented on the show: (1) 1907 Thomas Flyer; (2) 1911 Mercer Raceabout; (3)1933 Pierce Arrow; (4) 1964 Mustang; (5) 1934 Chrysler Airflow; (6) 1949 Cadillac Coup de Ville; (7) 1953 Corvette; (8) 1936 Cord 810; (9) 1909 Model T Ford; (10) and the choice of the experts -- the greatest car ever made, the 1929 Duesenberg Model J. Russell comment: If you go to Las Vegas, be sure to visit the auto exhibit at the Imperial Palace. They feature the greatest collection of "Dusies" in the world, and it's a breathtaking collection.

GOLD: Today we're dealing with a very old bull trend (and I'm talking about the bull market in stocks). We're also dealing with a new bull trend (and I'm referring to the bull market in gold). Consequently, I've been giving a lot of space in recent Letters to the new trend. Why not -- I think gold is where the future big profits lie, not in the overpriced stock market.

It's strange, but even "gold-bugs" don't know very much about gold. So let's talk a bit about the "mysterious" yellow metal. The simple facts about gold are: (1) gold is probably the prettiest of all metals; (2) gold is scarce; (3) gold is the only true money.

Gold also possesses a number of outstanding physical characteristics. For one, gold is the most malleable of all metals. One ounce of gold can be hammered into a translucent sheet covering 100 square feet five millionths of an inch thick. Incredibly, 1000 of these gold sheets would make up the thickness of one newspaper page. As for ductility, a single ounce of gold can be drawn out in a wire 50 miles long.

There's more -- gold doesn't tarnish. You can put a few gold coins or a gold ring away for your great, great grand-children, and when the kids fish them out of the vault in the year 2100, that gold will be as shiny and beautiful as the day it was made.

Gold is one of the heaviest of all metals. It has a specific gravity of 19.3, which means that it is 19.3 times as heavy as an equal volume of water. Ever hold 25 gold coins in the palm of your hand? I mean they are heavy.

Gold is quite scarce. All the gold ever mined in world history would weigh only 112,000 metric tons. Consider this: in 1992 the US steel industry poured an average of 10,500 tons of steel an hour. In comparison, in 1992 the entire gold industry produced a total of 2,000 tons of gold -- and that was for the entire year 1992.

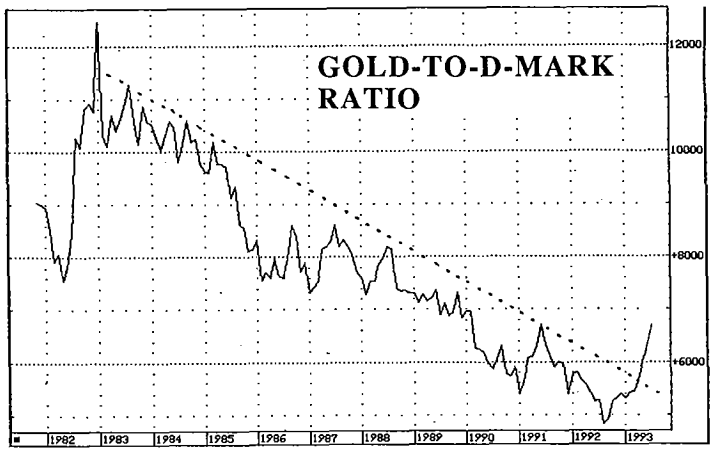
The world's annual production of gold is increasing at a rate of roughly 1.5% to 2% a year. According to the International Monetary Fund, money aggregates (M-1) for the industrial countries alone increased at a rate of 7.1% in 1990, 6.7% in '91 and 8.8% in '92.

So nations are "creating" paper money at three or four times (probably more) the rate of the production of gold (and Lord knows how much paper money is being ground out by the undeveloped nations). Conclusion: gold (real money) is being swamped by an ever-increasing ocean of paper and paper credits.

However, and this is a very BIG however, it's not supply and demand production that moves gold in a bull market. Yes, gold production may have a little to do with it (for instance, jewelry demand is currently taking all the gold currently being produced), but the real mover for gold is INVESTOR'S SENTIMENT.

For instance, when gold was rocketing up in 1979-80 nobody cared how much new gold was being taken out of the ground. What the buyers cared about was that inflation was extremely high and gold was the ultimate inflation hedge. Again, when the gold stocks surged higher during the early '30s it wasn't a question of how much gold was being mined. During the early '30s the price of everything was sinking due to deflation, but the price of gold had been raised. The mines' labor costs were plunging but their product, gold, had risen in price by 50% (Roosevelt raised the price of gold in an effort to reinflate the economy).

COMPETITION: Since 1983 gold has had a competitor. The competitor has been the mighty Deutschemark. The D-mark, backed by the power of the conservative Bundesbank, was taken to be as good as gold. Furthermore, the D-mark paid an attractive rate of interest.



For 10 years the D-mark served as a practical substitute for gold. That was then, this is now. The accompanying chart tells a dramatic story. Here we see the Gold/D-mark ratio, and over the past few weeks we see the ratio breaking out of a long, 10-year declining trendline -- in favor of gold.

So the D-mark is no longer the great island of safety. At last it's being by-passed by gold.

Furthermore, under the pressure of an expanding money supply and a huge deficit and inflationary worries, the D-mark is now coming into question as the "power-currency" of Europe. The talk of the FOREX traders is that the French franc may be the new leader. Paper currencies rise and paper currencies fall (yes, even the D-mark can fall), but gold has outlasted every paper currency and every paper-producing central bank in history.

Mark Ends Its Reign as Anchor of EC Currencies

Neighbor Members Get The Breathing Room to Lower Interest Rates

By Tom Buerkle
International Herald Tribune

COPENHAGEN — European officials declared Tuesday that the Deutsche mark was ceding its role as Europe's anchor currency and that the unprecedented change gave Germany's

As I detailed in the last Letter, Europe is in recession, Japan is in recession, most of the world (with the exception of China and the "Tigers") is in recession. And the US, under the auspices of President Clinton and company, will probably soon sink into recession.

What would be the US' reaction to rising unemployment and a resumption of recession? Easy, the reaction to any renewed slide into recession would be fiscal stimulation on a massive scale. And massive stimulation, in turn, will produce a sinking dollar and a rising price for gold.

I include here the daily chart for gold. Gold spiked up a total of $58 between March 12 and May 28. Next we saw a correction down to the mid-360s. Since then gold has been creeping higher. The first target is the (spot) 382-84 level. If that is breached, I look for gold to attack the 400 level.

I want to repeat again that this is the early resumption of the gold bull market. Gains in these early stages of any bull market are erratic, slow, difficult and almost always frustrating. They require patience. The bull market at this stage "wants" to take gold higher with as few investors aboard as possible.

That's the way bull markets work. In their early stages they don't give you obvious incentives -- they don't provide bullish news, and they don't give you a smooth ride to higher prices. You wait, you sweat, you wonder, you earn every point that you get. C'mon, if it was easy, everybody and his brother would get aboard and they'd all be making money. But it just doesn't work that way.

Another factor. The precious metals don't usually do well during the summer. Don't ask me why. A study of the price action just tells us that summer is not "happy time" for the precious metals. So I'd say that if gold and silver tend to do well during June to October, that's a very bullish sign.

A study of history also tells us that gold (and gold stocks) tend to establish an important low during the fourth quarter of the year. Therefore, if gold holds up this summer and it doesn't lose a substantial amount this fall, we know we're looking at a powerful bull market.

So again I'll say, this is the difficult part of the gold bull market. This is the "white knuckle" phase. Later, when the news is out, when the reason for buying gold becomes obvious, when the public decides that gold, not bonds or stocks, is the place to be -- that will be the easy phase.

But by that time the price of gold items will be substantially higher than they are today. Bargain-basement time will be past. Let me put it this way -- if gold ever gets to 1,000 your plumber and your shoe repair man and your broker will be telling you what a great buy it is.

You know it's amazing -- the Fed and banks manufacture dollars by decree. Dollars aren't the product of anyone's labor. Nobody at the Fed sweated for dollars. Dollars are legal tender to pay off debts, but why? Why, well because our government says they're legal tender.

They tell us that dollars are real money, and what's worse -- we believe them.

But gold is money with intrinsic value. Gold can't be created out of thin air. Gold is brought out of the ground by men's labor. Mining is expensive, and getting gold out of the ground is expensive. Therefore, gold production is limited because gold is scarce and because it takes entrepreneurship and capital and labor to retrieve it.

Does it make sense that men are willingly trading scarce tangible gold for paper "money" that is produced by the carload by our government? Ah, that's one of the great mysteries of today. But times change. Listen, I was buying one ounce gold St. Gaudens coins for $70 each back in 1975. I sold them for $700 a piece five years later. Why did the coins sell for $70 in 1975? Because people had faith in the dollar and they were told that gold was a "barbarous relic."

Is gold at today's $375 a "barbaric relic"? No, but people would rather have 380 one-dollar bills than an ounce of gold. That will change in time, as the bull market in gold gathers steam and as the US government continues to print billions of new paper dollars.

Last week Faye and I went to the big Del Mar County Fair. At the fair (no we didn't eat any cinnamon rolls or battered deep-fried swirled potatoes) they had an exhibit that fascinated me. It was the actual first house built in Del Mar city. The well-made little wooden house had five rooms, and was maybe 1,000 square feet. It was built in 1888 and the cost -- the cost was $600. A very livable house for $600? Gad, I thought, it's unbelievable how far the purchasing power of the dollar has fallen.

LATE NOTES: Gold, rising nine dollars on July 1, broke out of its consolidation -- to record a new high for the move. The background is perfect for the precious metal bull market -- declining global interest rates, nations moving to stimulate, no signs of inflation (yet), and silence or universal skepticism regarding the gold advance. Actually, it's almost comical to read the goofy, misinformed explanations for the gold rise in the *NY Times*, the *WSJ* and other media outlets.

Unemployment, as I've stressed, will be the "Nightmare of the Nineties," and world governments will offer only one way to fight it -- inflation in the form of monetary stimulation and lower interest rates. Note: IBM announces that instead of a scheduled 25,000 layoffs, they are raising that figure to 50,000.

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